

# **CITY AUDITOR'S OFFICE**



## **AUDIT OF INSURANCE SERVICES – EMPLOYEE BENEFITS**

**Report CAO 502-0203-05**

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**RADFORD K. SNELDING, CPA, CIA, CFE**

**CITY AUDITOR**

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# **AUDIT OF INSURANCE SERVICES - BENEFITS**

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### **BACKGROUND**

Insurance Services is a division in the Department of Human Resources. Insurance Services has three operational units: Employee Benefits, Safety/Liability/ADA, and Worker's Compensation. This audit focused on the Employee Benefits unit of Insurance Services. Insurance Services was responsible for managing \$10.9 million in claims in 2001. Employee Benefits has a benefits analyst and two benefits specialists.

The City of Las Vegas (CLV), like most employers, provides its employees a variety of benefits that have developed over the years based on cost, negotiations with the City Employees Association (CEA), and to remain competitive with other local governments and employers. The City of Las Vegas is self-insured and uses a contracted Third Party Administrator (TPA) for claims processing, customer service, and problem resolution. Employees contact the TPA when questions arise related to their benefits and billing. Employee Benefits becomes involved if an issue cannot be resolved between the TPA and employee.

### **OBJECTIVES**

This audit was part of the City Auditor's Office annual audit plan. Our objectives included the following:

- Review and evaluate efficiency, effectiveness, and adequacy of operational, financial, and system controls;
- Review compliance with policies and procedures; and
- Determine whether city assets and data are used appropriately and safeguarded from loss.

### **SCOPE AND METHODOLOGY**

Our audit was performed in accordance with generally accepted governmental auditing standards. We evaluated the efficiency and effectiveness of Employee Benefits. Audit procedures included:

- Reviewing policies and procedures;
- Reviewing the City Charter;
- Interviewing management, staff, and vendors;
- Observing operations; and
- Analyzing operational data.

## **FINDINGS AND RECOMMENDATIONS**

The following issues were identified during the audit. While other issues were identified and discussed with management, they were deemed less significant for reporting purposes.

### **1. GROUP INSURANCE FUND BALANCE RESERVE**

#### **Criteria:**

- Established fund balance reserves protect against unforeseen increases in insurance claims and medical costs.

#### **Condition:**

- The City's Group Insurance Fund (an Internal Service Fund) is used to account for monies collected from city departments and employees to be expended for claims for medical, dental and vision services provided to employees and their dependents.
- While the Fund currently has a positive unreserved fund balance, it does not have a formal fund balance reserve.
- Two other Insurance Internal Service Funds (Worker's Compensation Insurance and Liability Insurance) have formal fund balance reserves for benefits, claims and insurance premiums.
- In addition to paying the employer portion of the established health insurance premiums as determined by the City's third party administrator, the City contributed over \$4.4 million and \$4.6 million in fiscal years 2001 and 2002, respectively, to the Group Insurance Fund to maintain a positive unreserved fund balance.
- Current health insurance premiums appear to be inadequate and they do not include a component to build a specific Group Insurance fund balance reserves as evidenced by the need for funding from the City above the established employer and employee premiums.
- Prior to 2003, actuaries employed by the Plan Administrator established the health insurance premiums. Insurance Services hired an independent actuary to establish premiums for 2003.
- Neither Insurance Services nor Finance has requested the actuaries to include the building of a formal reserve within their calculations.

#### **Cause:**

- Issue not adequately addressed by City management.

#### **Effect:**

- Potential for inadequate funding of claims within the Group Insurance Fund.
- Potential need for additional unplanned funding by City.

#### **Recommendations:**

1. Finance should adopt a formal fund balance reserve for the Group Insurance Fund.
2. Insurance Services should annually hire an independent certified actuary:
  - To establish employer and employee health insurance premiums adequate to cover medical costs.
  - To determine an appropriate fund balance reserve for the Group Insurance Fund and a

premium component for building the recommended fund balance reserve.

## **2. CONTRACT REQUIREMENTS**

### **Criteria:**

- The City should comply with the terms within contractual agreements or work toward having the terms changed if the City does not agree with them.

### **Condition:**

- By contract, the City's self-funded health insurance plan is obliged to pay 100% of health, dental, and vision insurance coverage for each employee and 50% of the actual cost of dependent insurance coverage costs.
- Insurance Services has not determined what percentage of the actual cost of dependent insurance coverage costs the City is paying or considered this in determining City employee premiums.
- The actuary hired by the City has not considered these contractual requirements in calculating recommended City employee premiums.
- Insurance Services management stated that the verbiage within the contract regarding dependent insurance coverage costs is inappropriate, as it does not reflect current practice.

### **Cause:**

- Issue not adequately addressed by City management.

### **Effect:**

- The City may not be complying with the contract.
- The City may be paying more towards medical claims than required under the contract.

### **Recommendations:**

1. Insurance Services should complete an analysis of insurance costs paid on behalf of dependents to determine whether the City is in compliance with the contract.
2. Insurance Services should ensure that the actuary considers the contract requirements when determining insurance premiums.
3. Insurance Services should adjust the verbiage as needed and modify the contract to reflect the actual method of determining insurance premiums.

## **3. INSURANCE PLAN COMPONENTS**

### **Criteria:**

- Health insurance plan components should continually be reviewed to ensure the cost-benefit of the service makes good financial sense for the City and the employee.
- Insurance expenses can be reduced through contract terms that give the insured incentives to avoid and limit expenses.

**Condition:**

- Health costs continue to increase for the City.

**Cause:**

- Limited incentives in place to encourage living a healthier lifestyle or limit employee usage of medical services.

**Effect:**

- Increasing health insurance costs to the City.

**Recommendations:**

1. Insurance Services should evaluate alternatives to the current health plan such as consumer driven healthcare and HPN (an HMO - Health Maintenance Organization), which will continue to provide quality healthcare to employees and significantly reduce the City's financial exposure.
2. Insurance Services should consider, evaluate, and document options which provide employees incentives to live healthier lifestyles (non-smokers, going to a gym) and limit usage of medical services.

#### **4. HIPAA**

**Criteria:**

- Nonfederal governmental employers that sponsor a self-funded group health plan may elect to exempt their plan from some HIPAA provisions.

**Condition:**

- Title I of the Health Insurance Portability and Accountability Act of 1996 (HIPAA) protects health insurance coverage for workers and their families when they change or lose their jobs.
- Nonfederal governmental employers can exempt themselves from Title I of HIPAA. By doing so, the employer can:
  - ▶ Place limitations on preexisting condition exclusion periods.
  - ▶ Have special enrollment periods.
  - ▶ Select who can participate in the health plan based on medical history.
  - ▶ Set standards relating to benefits for mothers and newborns.

**Cause:**

- Insurance Services – Employee Benefits Management has not evaluated this option and its impact.

**Effect:**

- Cost savings to most employees and the City.

**Recommendation:**

1. The City Manager's Office in conjunction with Human Resources Management should evaluate and document the benefits of opting out of Title I of HIPAA.

**5. MONITORING OF PERFORMANCE**

**Criteria:**

- In accordance with the Agreement between the City and its TPA, the following quarterly performance standards must be met or the TPA is subject to a 5% quarterly administrative fee penalty for each standard not achieved, Claims Processing Time, Claim Payment/Processing Accuracy, and Customer Survey Results.

**Condition:**

- Subsequent to the commencement of this audit, the TPA was released and Insurance Services chose a new TPA.
- Since inception of the contract with its TPA in January 1, 2000, the City has relied upon data from the TPA as to whether the TPA was in compliance with the contractual performance standards.
- Insurance Services has not monitored compliance with the contractual performance standards except for hiring an external auditor to perform a claims review.
- Insurance Services accepted new insurance cards in lieu of penalties but there is no documentation showing the cost of the cards versus the penalty for the period.
- In May 2002, an external claims auditor performed a claims audit of the TPA for the two quarters ending March 2002. As a result of the findings of this audit, Insurance Services assessed the TPA a penalty of \$28,691.29 or 15% of administrative fees for not achieving the established performance standards during the period under audit.
- The City has experienced additional performance problems with the TPA including incomplete or inaccurate check reconciliation and inadequate data for proper recording of claims expenditures in the general ledger.
- Insurance Services has assessed the TPA penalties without sufficient documentation.

**Cause:**

- Insurance Services has not independently monitored the TPA's tracking and meeting of the contractual performance standards.

**Effect:**

- City has not received the stipulated 5% penalty for all quarters of non-compliance.
- Quality of service is substandard.
- Dissatisfied employees.

**Recommendations:**

1. Insurance Services should require the TPA to pay 15% of the quarterly administrative fees for the periods of noncompliance with contractual standards.
2. Insurance Services should implement measures to monitor the performance standards

specified in the TPA contract.

3. Insurance Services should require that the TPA make penalty payments in a timely manner once non-compliance has been identified.

## **6. DATA ANALYSIS**

### **Criteria:**

- In order to maintain data integrity, data should be checked when it is entered into a system for completeness and accuracy. Data integrity is maintained by ongoing comparisons and verifications as data is processed.

### **Condition:**

- Data integrity refers to the validity of the data.
- If invalid data is entered into a system, the output will also be invalid. GIGO – garbage in, garbage out.
- Insurance Services does not perform tests to monitor the accuracy and completeness of employee, retiree, or dependent information provided to the TPA.
- The City database had 4,887 employees, retirees, and dependents and the TPA database has 4,879 members. 404 discrepancies exist between the databases including:
  - Birthday information not included in one or both systems
  - Birthdays do not match between systems.
  - Employees, retirees, and dependents are in one system but not in the other system.
  - Social Security numbers do not match between systems.

### **Cause:**

- Insurance Services is not adequately reviewing or monitoring system information.

### **Effect:**

- The TPA could be overpaying or underpaying on claims.

### **Recommendation:**

1. Insurance Services should regularly perform reconciliations and data analysis with the TPA to ensure the accuracy and completeness of member information and claims information.

## **7. REVIEW OF TPA CHECK REGISTER**

### **Criteria:**

- Proper review and scrutiny of check registers can help identify payment errors or irregularities.

### **Condition:**

- Insurance Services receives a weekly check register from the City's TPA showing claims checks to be issued.



- The check register only includes claim numbers, dates of service, payee, and total due. Names of employees and the nature of service are withheld by the City's TPA.
- Insurance Services performs a limited review of the check register including keeping a running total of expenditures, tracking average monthly expenditures, and reviewing specific providers.
- The recent external claims audit identified a wide range of significant claims processing errors by the TPA showing the need for increased monitoring of the TPA by the City. The City may have identified repeated processing errors earlier with more detailed monitoring of individual claims.

**Cause:**

- Limited information provided on the check register.

**Effect:**

- Potential payment errors or irregularities.

**Recommendations:**

1. Insurance Services should work with the claims auditor to develop ways to monitor and review claim information.
2. Insurance Services should request more detailed check registers from the TPA to allow for a more detailed analysis of the transactions.
3. Insurance Services should increase its monitoring and scrutiny of the weekly claims payment check register by establishing and performing more detailed review procedures.

## **8. EMPLOYEE BENEFIT PLAN DOCUMENT AVAILABILITY**

**Criteria:**

- Employee benefit plan documents should be readily accessible to employees for their use in understanding plan benefits and in reviewing the accuracy of claim statements and invoices.

**Condition:**

- While a summary of the City's medical benefits program is available to employees on the City's intranet site, the City's Employee Benefit Plan Document (Plan Document) is not currently accessible on the City's intranet site.
- According to Insurance Services, the Plan Document is available to employees and retirees at Insurance Services.
- The Plan Document is distributed to employees at employee orientation.
- Updates to the Plan Document are provided to employees, but an updated version of the Plan Document has not been distributed to employees.
- Insurance Services did provide a copy of the Plan document to all employees for 2003.

**Cause:**

- Potentially inadequate employee benefit Plan Document.

**Effect:**

- Potential for confusion by employees on Plan benefits.
- Additional questions to Insurance Services.

**Recommendations:**

1. Insurance Services should develop a process to inform employees annually of Plan Document changes and availability.
2. Insurance Services should make the most recent version of the Plan Document available to employees in a variety of ways such as via the Internet, the intranet, and available for pickup at Insurance Services.

## **9. PAYMENT PROCESSING**

**Criteria:**

- Las Vegas Municipal Code Section 4.04.020 states, "All revenues and other cash receipts collected by any City department, court or agency must be receipted at the time received and deposited with the City Treasurer by the close of the following business day."
- Finance and Business Services Cash Handling Policy states, "all revenue collections, regardless of the amount, shall be deposited intact within 24 hours."

**Condition:**

- COBRA and retiree insurance payments received by Insurance Services are stored in a cash box in a locked drawer until posted to the City's cash receipting system. Once payments are input into the system, they are delivered to the City Treasurer's Office for inclusion with the day's deposit.
- Payments received by Insurance Services staff are not typically posted to the cash receipting system or deposited in accordance with the guidelines established by the Municipal Code and the Cash Handling Policy.
- Insurance Services collects approximately \$9,000 monthly in COBRA and retiree insurance payments. A review of the cash box included checks and money orders totaling \$1,738.80, which were 60 to 90 days old.

**Cause:**

- Few checks are received daily.
- Posting of payments to cash receipting system is not a high priority.

**Effect:**

- Non-compliance with the Municipal Code and the Cash Handling Policy.
- Increased risk of loss.

**Recommendation:**

1. Insurance Services should process all COBRA and retiree insurance payments in accordance with the Municipal Code and the City's Cash Handling Policy.

## **10. DEFERRED COMPENSATION**

### **Criteria:**

- Ongoing review of fees, services provided, and customer service, helps ensure quality.

### **Condition:**

- City employees currently have the option of two deferred compensation (457) plans.
- The City has never gone out to RFP for deferred compensation plans.
- Both plans offer investments from major mutual fund investment management companies such as American Century, Putnam, Janus, etc.
- The City does not pay any fees for the deferred compensation plans.
- The plan managers earn their money from fees charged to employees in the funds and/or rebates from the mutual fund company.
- The plan managers have a transfer out fee for employees transferring funds out of their plan to other plans.
- Investment product fees are higher for products purchased from our current plan managers than if purchased directly from the investment management companies offering the same product.

### **Cause:**

- Management has not issued an RFP for deferred compensation programs to determine which would provide the best value and options to employees.

### **Effect:**

- City employees may be paying more than necessary for their investments since the same or similar investments could be obtained at a lower cost through other 457 administrators (i.e. directly with investment management companies).

### **Recommendations:**

1. Insurance Services should consider, evaluate, and document an RFP for deferred compensation plan managers to make an educated decision of which plan managers offer the best value and lowest fees for City employees and decide whether to add, remove, or retain the current plan administrators.
2. Insurance Services should compare deferred compensation plan fees offered by the current plan administrators to those of investment management companies.
3. Insurance Services should evaluate companies offering no-load funds as an option for deferred compensation.

## **11. MEDICAL AND DEPENDENT CARE FLEXIBLE SPENDING ACCOUNTS**

### **Criteria:**

- Formal signed contracts should exist detailing the terms and conditions between the parties exchanging services.

**Condition:**

- The City utilizes Section 125 of the Internal Revenue Code by allowing employees to choose benefits that best fit their personal situation. It makes possible for employees to contribute to their fringe benefits on a "Pre-Tax" basis, and to set aside via voluntary deduction additional "Pre-Tax" dollars to pay for out-of-pocket Dependent Care and/or Medical Expenses through separate Flexible Reimbursement Spending Accounts.
- According to Insurance Services, the current 125 plan administrator became the provider of this service in July 1997 when the previous provider had financial difficulties and there was concern from Human Resources that City employees could possibly lose their funds.
- The City's 125 Flexible Benefit Plan Administrator does not have a formal, signed contract with the City.
- Employees pay \$2.31 per pay period for this service. The City does not pay anything to provide this service.
- According to the vendor, 90% of corporations pay the monthly fee for their employees.

**Cause:**

- Lack of proper monitoring of contract files.
- City does not have a formal agreement with the 125 plan administrator

**Effect:**

- City employees may be paying too much for this service.

**Recommendations:**

1. Insurance Services should develop a contract with its current 125 plan administrator to ensure the agreed upon terms are clearly defined.
2. Insurance Services should consider, evaluate, and document an RFP for 125 plan administrators.
3. Insurance Services should review 125 plans and determine how it can best provide this benefit to employees at the lowest cost.
4. Insurance Services should regularly promote the benefits of a 125 plan.

## **12. LIFE INSURANCE**

**Criteria:**

- Programs promoted by the City on behalf of outside vendors should be monitored by city staff and issues timely communicated to employees.

**Condition:**

- The City provides most employees \$20,000 basic life insurance at no cost to the employees and provides executives with \$50,000 basic life insurance.
- Other municipal entities surveyed provide from \$5,000 to 250% of base pay.
- Supplemental life insurance is available to employees through an outside insurance carrier.
- The outside insurance carrier offered an open enrollment period starting January 1, 2002 and

ending on February 28, 2002 with guarantee issue amounts.

- The effective date of coverage was not communicated to employees.
- Not all supplemental policies received in a timely manner by employees.
- Payroll deductions for premiums for supplemental coverage did not begin until May 3, 2002.
- While premium payments are being collected, there has been no correspondence to employees from either the City or the insurance carrier regarding the insurance policies to employees and the insurance policies have not been distributed to employees.

**Cause:**

- Delays by insurance carrier due to use of new underwriter.

**Effect:**

- Confusion for employees.
- Employees do not have insurance policies for reference and safekeeping.

**Recommendations:**

1. Insurance Services should proactively monitor programs offered by vendors and keep employees informed when delays or problems occur.
2. Insurance Services should contact the supplemental insurance carrier to determine when the supplemental insurance policies are to be distributed.

### **13. OFFICE PROCEDURES**

**Criteria:**

- An updated office procedures manual is a helpful reference for new and current employees and can help communicate and encourage adherence to policies and procedures and prevent possible confusion or misunderstandings among personnel.

**Condition:**

- Lack of updated office procedures manual outlining the specific operations.
- Lack of awareness of office procedures manual.

**Cause:**

- Manual not updated and not distributed to employees.

**Effect:**

- Potential for misunderstandings of policies, procedures, and areas of responsibility.
- Lack of a reference manual for training new employees.

**Recommendation:**

1. Insurance Services should update the current office procedures manual, make employees aware of the manual, and keep it updated as needed.